

**DEPARTMENT OF INSURANCE****Legal Division, Conservation & Liquidation Bureau**

45 Fremont Street, 21st Floor  
San Francisco, CA 94105



**NOTICE OF PROPOSED EMERGENCY ACTION  
PURSUANT TO CALIFORNIA INSURANCE CODE SECTION 12921.7**

File No. ER-02-019089

January 14, 2002

**CONFLICT OF INTEREST CODE FOR THE CONSERVATION  
& LIQUIDATION OFFICE**

California Insurance Commissioner Harry W. Low hereby provides notice, pursuant to California Insurance Code Section 12921.7, that he will propose to the Fair Political Practices Commission the adoption of Title 10, Chapter 5, Subchapter 10, Article 1, Sections 2699.1 – 2699.7 of the California Code of Regulations on an emergency basis pursuant to California Government Code Section 11346.1(b) and Insurance Code Section 1035.2.

This Notice contains a description of the problem and the necessity for the regulations, an explanation of the justification for the adoption of the regulations on an emergency basis, and a copy of the proposed regulations.

This Notice is provided to every person, group, and association who has previously filed a request for notice of regulatory action with the Commissioner. Copies of the Notice are available at the Department of Insurance, 45 Fremont Street, 21<sup>st</sup> Floor, San Francisco, California, 94105.

The proposed regulations will be submitted to the Fair Political Practices Commission together with the rulemaking file not less than five (5) working days after the mailing of this Notice, as required by California Insurance Code Section 12921.7. Questions regarding this Notice should be directed to the following:

California Department of Insurance  
Legal Division, Conservation & Liquidation Bureau  
Attn: Jack Hom, Senior Staff Counsel  
45 Fremont Street, 21<sup>st</sup> Floor  
San Francisco, California 94105  
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**DESCRIPTION OF PROBLEM AND NECESSITY FOR REGULATIONS**

California Insurance Code ("CIC") Sections 1013, 1011, and 1016 provide statutory authority for the Insurance Commissioner to seize, conserve, and liquidate insurance companies if any are

in such condition that their further transaction of business would be hazardous to their policyholders, or creditors, or to the public.

Upon obtaining a court order to be appointed as the Conservator and/or Liquidator, the Insurance Commissioner must either rehabilitate the companies (and operate them as on going concerns) or must liquidate the companies. To assist him in rehabilitating or liquidating the companies, the Insurance Commissioner, in his capacity as the court-appointed Conservator and Liquidator, established the Conservation & Liquidation Office (“CLO”), which is comprised of insurance professionals managed by a Chief Executive Officer (“CEO”) and other officers (Deputy CEO, Chief Financial Officer, Reinsurance Officer, Claims Officer, and Chief Information Officer) and managers. The CLO officers and managers make decisions on a regular basis which affect the financial interests of the conserved or liquidated companies (and by extension, the ability of the conserved or liquidated companies to pay policyholders’ and creditors’ claims).

Prior to 2002, only the CEO and Deputy CEO were subject to state laws pertaining to conflicts of interest and financial disclosures, and that was only because the two incumbents in those positions were (are) state employees. On January 1, 2002, a new California statute (CIC Section 1035.2) went into effect which provides that the officers and employees of the CLO are subject to all conflict of interest provisions and financial disclosure requirements that would apply if they were employees of the California Department of Insurance (“CDI”). Further, the new CIC Section 1035.2 requires, prior to February 1, 2002, that the CDI promulgate and adopt a Conflict of Interest Code (regulations) pursuant to the provisions of Article 3 (commencing with Section 87300) of Chapter 7 of Title 9 of the Government Code, pertaining to the officers and employees of the CLO. Finally, the new CIC Section 1035.2 requires the CDI to promulgate and adopt these conflict of interest regulations as emergency regulations.

#### **JUSTIFICATION FOR ADOPTION AS EMERGENCY REGULATIONS**

There are currently fifty-four (54) companies (known as estates) in conservation or liquidation under the CLO’s management. For calendar year 2000, the estates generated approximately \$32,000,000 in annual revenue (from dividends and interest earned). The officers and managers of the CLO make daily decisions which have an impact on the interests of policyholders, creditors, and others interested in the assets of the estates. At present, there are no conflict of interest guidelines which define specific conflicts of interest and no financial disclosure requirements. Moreover, the normal process for promulgating and adopting conflict of interest regulations and financial disclosure requirements takes several months. Due to the size and scope of the CLO’s operations, the legislature determined it was necessary that the conflict of interest regulations and financial disclosure requirements be put in place by February 1, 2002.

These emergency regulations put in place specific conflict of interest guidelines and reporting requirements for the CLO officers, managers, and other key employees. Once these emergency regulations are in place, the CLO officers and managers can more easily determine whether they have a conflict of interest, or a potential conflict of interest, and disqualify themselves from the decision-making process, as appropriate. After the emergency regulations are in place, the Insurance Commissioner will proceed with the normal process for promulgating and adopting these regulations.

**TEXT OF THE PROPOSED REGULATIONS**

The proposed regulations are attached.

Dated: January 14, 2002

HARRY W. LOW  
Insurance Commissioner

By: /S/  
LORRAINE JOHNSON  
Assistant Chief Counsel